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State of Utah v. C. Dean Larsen : Reply Brief

Utah Supreme Court

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BRIEF

#2

IN THE UTAH SUPREME COURT

STATE OF UTAH,	:	
Plaintiff/Respondent,	:	Supreme Court No. 920114
v.	:	Court of Appeals No. 900473-CA
C. DEAN LARSEN,	:	Category No. 14
Defendant/Petitioner.	:	

REPLY BRIEF OF THE PETITIONER

ON WRIT OF CERTIORARI
TO THE UTAH COURT OF APPEALS

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REPLY BRIEF OF THE PETITIONER

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ON WRIT OF CERTIORARI TO THE
UTAH COURT OF APPEALS

ARGUMENT

I. Scienter is an Independent Element of a Criminal Violation of Sections 61-1-1(2) and 61-1-21

The State does not question the decree of Utah's legislature that a "general purpose" of the Utah Uniform Securities Act is to coordinate the interpretation of the Utah Act with *the* related federal regulation. See Utah Code Ann. § 61-1-27. Further, the State presents nothing to dispute that a violation of Rule 10b-5, the model for what became Utah Code Ann. § 61-1-1, requires proof of scienter. Finally, the State never questions, from a policy view, the importance of the scienter requirement and the significance of aligning the construction of Section 61-1-1 with federal court interpretation of Rule 10b-5.

Nonetheless, the State urges the Court to ignore the independent scienter element of Rule 10b-5 in construing section 61-1-1. The State argues that the unrelated congressional intent of § 17(a) of the 1933 Act, 15 U.S.C. § 77q, which does not require scienter, should be substituted for the legislative intent for § 10(b) of the 1934 Act, 15 U.S.C. § 78j, which was the enabling statute for Rule 10b-5, and which requires scienter. State's br. at 12-20. The State suggests alternatively that because neither the term "scienter" nor its components are expressly enumerated among the terms of sections 61-1-1 and 61-1-21, the Court should not recognize the *independent* scienter element of Rule 10b-5, which was the pattern for section 101 of the Uniform Securities Act and, in turn, for section 61-1-1. The State's arguments ignore the purpose of the Utah Act and misconstrue the Supreme Court's decisions.

A. Section 61-1-1 Is Based On Rule 10b-5, Not on Section 17(a)

The State does not question that a violation of § 10(b) and Rule 10b-5 requires proof of scienter, as the Court in Ernst & Ernst v. Hochfelder, 425 U.S. 185, 201, 212-14 (1976) explained.[1] Yet, the State charges that Mr. Larsen "erroneously

[1]The State implies that because Hochfelder was a civil action, the scienter element would not apply in a criminal prosecution. States br. at 7. However, that Hochfelder was a civil and not criminal case, is not significant as the Supreme Court explained: "In our view, the rational of Hochfelder

(continued...)

views Hochfelder in isolation" and fails to give "due weight" to one other Supreme Court case, Aaron v. S.E.C., which discussed separately § 17(a) and Rule 10b-5. State's br. at 13. The State reasons this way: because *language* for Rule 10b-5 was borrowed in part from § 17(a) of the 1933 Act, then the *intent* of § 17(a)(2), as defined in Aaron, must govern or be "at least as instructive" as the Hochfelder ruling, in construing Rule 10b-5, the model for what became section 61-1-1 of the Utah Act. State's br. at 14-16. Then, citing only the portion of Aaron that analyzes § 17(a), the State concludes that "the Supreme Court case law interpreting related federal regulation" does not dictate that section 61-1-1 be construed to require proof of scienter. State's br. at 15.[2]

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[1](...continued)
ineluctably leads to the conclusion that scienter is an element of a violation of § 10(b) and Rule 10b-5, regardless of the identity of the plaintiff or the nature of the relief sought." Aaron v. S.E.C., 446 U.S. 680, 691 (1980).

[2]The State now employs the phrase "interpreting related federal regulation" which closely resembles the important language of purpose in section 61-1-27, leaving the incorrect impression that § 17(a) is "the" federal regulation related to section 61-1-1. State's br. at 15. The State builds on this misconception, stating that § 17(a), "*through* rule 10b-5 was *a model* for section 101 of the Uniform Securities Act and therefore section 61-1-1." State's br. at 16 (emphasis supplied). Contrary to the impression left by these carefully worded statements, the truth is that Rule 10b-5 alone, and not § 17(a) of the 1933 Act, is *the* federal regulation related to section 61-1-1. See Uniform Securities Act § 101, Official Comment, reprinted in Louis B. Loss, Commentary on the Uniform Securities Act, 6 (1976); Petitioners br. at 7-10.

Unmasked, the State's argument is an attempt to switch the congressional intent of § 10(b) of 1934 Act (and thus, of Rule 10b-5), with the very different intent of § 17(a)(2) of the 1933 Act. However, the State's syllogism is defective and misconstrues the Supreme Court decisions; here, the eye is quicker than the hand.

1. Aaron v. S.E.C.

Apart from the inherent defect in logic in the State's position,[3] Aaron does not condone the State's intent-switching analysis. The Aaron court confirmed that the *intent* of Rule 10b-5 is discerned from the language and congressional intent § 10(b), the statute under which Rule 10b-5 was promulgated. Aaron, 446 U.S. at 691 ("since the Commission's rule-making power was necessarily limited by the ambit of *its statutory authority*, the [Hochfelder] Court reasoned that Rule 10b-5 must likewise be restricted to conduct involving scienter.") (emphasis supplied). See also Petitioner's br. at 7-10.

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[3]It does not follow that by borrowing *language* from § 17(a)(2) (a statute allowing prosecution without proof of scienter), for use in Rule 10b-5 (a rule promulgated under a statute requiring proof of scienter), that the legislative *intent* of § 17(a) would somehow override known congressional intent for § 10(b) and Rule 10b-5. Moreover, the different intents of § 10(b) and § 17(a) are incompatible; they cannot be combined to form a useful guide for interpretation. The State's argument, which ignores congressional intent for Rule 10b-5, fails to reconcile this.

The Aaron Court, like the Court in Hochfelder, construed Rule 10b-5 without substituting the legislative intent of § 17(a)(2), as the State does. State's br. at 14-16. See Aaron, 446 U.S. at 689-91; Hochfelder, 425 U.S. at 197-214. Similarly, the Aaron Court construed § 17(a) independently, according to its own legislative history and language. Aaron, 446 U.S. at 695-700. The Supreme Court found no "expression of congressional intent in the legislative history" of § 17(a) that scienter was required under § 17(a)(2) and (3). Id. at 697.[4] On the other hand, the Aaron Court reaffirmed that the legislative history and plain meaning of the language of § 10(b), and the structure of the 1933 and 1934 Acts, show that scienter is an element of a Rule 10b-5 violation. Id. at 690-91, 695 ("the controlling precedent here is . . . Hochfelder. Accordingly, we conclude that scienter is a necessary element of a violation of § 10(b) and Rule 10b-5").

In short, contrary to the State's contention, the Supreme Court cases construing the intent of Rule 10b-5 and § 17(a), including Aaron (and Dirks v. S.E.C., 463 U.S. 646 (1983), which the State overlooks), do not authorize switching the congressional intent of § 17(a) with the intent of § 10(b) to

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[4]The Court, however, in determining the intent necessary to warrant injunctive relief, went on to note that "[t]his is not to say, however, that scienter has no bearing at all on whether a district court should enjoin a person violating or about to violate § 17(a)(2) or § 17(a)(3)." Aaron, 446 U.S. at 697, 701.

construe Rule 10b-5 and provisions patterned after it such as section 61-1-1.[5]

2. The State's Authorities

This is unchanged by other decisions the State cites. Neither State v. Temby, 108 Wis. 2d 521, 528-29, 322 N.W.2d 522, 526-27 (1982) nor People v. Whitlow, 89 Ill. 2d 322, 324-35, 433 N.E.2d 629, 634 (1982), which construed "61-1-1(2)-type" provisions, even cite Rule 10b-5, yet alone construe it with the intent of § 17(a). State's br. at 16. Temby, which does not mention section 101 of the Uniform Act, implies that the court relied on § 17(a) as a model for Wisconsin simply based on *language* similarity. 322 N.E.2d at 526 n.1. Whitlow is no different. 433 N.E.2d at 633-34 (the court concluded that § 17(a) is "closely analogous" to the statute at issue). These cases say nothing of congressional intent in applying Rule 10b-5.

The same is true of the State's remaining authorities. State's br. at 17-18. As previously explained, many of these state decisions are based on statutes lacking the legislative purpose that guides construction of section 61-1-1 of the Utah Act. See Utah Code Ann. § 61-1-27; Petitioner's br. at 13-14.

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[5]The State also attempts to divert Court attention from the congressional intent underlying Rule 10b-5 by picking at Rule 10b-5, noting that it was "hastily drafted," and discounting Hochfelder, saying that the Supreme Court did not "thoroughly analyze" the *language* of Rule 10b-5, all as though congressional intent were not at issue. State's Br. at 14.

Other decisions make no mention of section 101 of the Uniform Securities Act, of the legislative intent of Rule 10b-5 and of Hochfelder. Petitioner's br. at 13-14.[6] Thus, while such decisions, which collide with Hochfelder, may provide useful authority to construe laws based upon § 17(a), they do not assist states like Utah where the statutory counterpart is Rule 10b-5. See State v. Puckett, 6 Kan. App. 2d 688, 634 P.2d 144 (1981), aff'd, 230 Kan. 296, 640 P.2d 1198 (1982); People v. Terranova, 38 Colo. App. 476, 563 P.2d 363, 365-66 (1977).

The State also cites United States v. Chiarella, 588 F.2d 1358, 1370 (2d Cir. 1978), rev'd, 445 U.S. 222 (1980), and United States v. Charnay, 537 F.2d 341, 351-52 (7th Cir.), cert. denied, 429 U.S. 1000 (1976), implying that these cases reject the scienter element in Rule 10b-5 prosecutions. State's br. at 19.[7] This argument is defective on two counts: First, the State artificially narrows its definition (and analysis) of

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[6]Even the State appears to agree that the persuasiveness here of such state court decisions depends on the applicability of Hochfelder. State's br. at 18 (arguing that while the state court decisions it cites may conflict with Hochfelder, Hochfelder should not be viewed as "controlling authority"). And, the State does not reconcile the divergent analyses of these cases with the plain legislative purpose of the Utah Act and the known legislative intent of Rule 10b-5, the ultimate model for section 61-1-1.

[7]The court in Charnay relied on pre-Hochfelder authority which, to the extent it did not require proof of scienter, now is of little value. 537 F.2d at 351-52; Hochfelder, 425 U.S. at 212-14.

"scienter" to "the intent to defraud." State's br. at 5-6 n.2. Such intent is only one alternative proof requirement of the scienter element in a Rule 10b-5 prosecution. See Hochfelder, 425 U.S. at 193 n.12 (scienter embraces the "intent to deceive, manipulate, *or* defraud").

Second, and contrary to what the State implies, Chiarella does not retreat from the scienter requirement of Hochfelder. Chiarella held that the trial court's instruction omitting intent to defraud was proper where the trial court chose instead to instruct the jury that it must not find the opposite of such intent; i.e., that the defendant acted deliberately, "and *not* as a result of 'innocent mistakes, negligence, or inadvertence or other innocent conduct.'" 588 F.2d at 1370 (emphasis supplied). The effect is synonymous.

By requiring the jury to find that Chiarella's conduct did not result from negligence or other innocent conduct, the Chiarella court only told the jury that it could not convict if the accused acted in good faith -- the converse of intent to defraud. This instruction, like the instruction in United States v. Chestman, 704 F. Supp. 451, 459 (S.D.N.Y. 1989), rev'd, 947 F.2d 551 (2nd Cir. 1991), was a proper alternative scienter instruction. See Dirks, 463 U.S. 646, 674 n.11 (1983) (Blackman, J. dissenting) ("Moreover, if the insider in good faith does not believe that the information is material or non-public, he also

lacks the necessary scienter. In fact, the scienter requirement functions in part to protect good faith errors of this type (citations omitted)).[8]

Unlike the jury charge given in Chiarella, Mr. Larsen's instruction on good faith was refused. See Larsen's Requested Instr. No. 30 (R.1381).[9] And, the alternative definitions of the scienter element, including the components of good faith provided in Chiarella, were not instructed, contrary to the State's contention. State's br. at 19 (saying that Chiarella upheld jury instructions "similar" to those given at Mr. Larsen's trial). The jury here was told that it could find a violation of

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[8]After citing Chiarella and Chestman, which confirm that a Rule 10b-5 violation cannot be predicated on innocent mistake, negligence or inadvertence, the State inconsistently argues that "a good faith defense is not applicable." State's br. at 21. This ignores the controlling Supreme Court decisions. See Hochfelder, 425 U.S. at 212 n.31; Dirks, 463 U.S. at 674 n.11. The State's citation to the pre-Hochfelder case Sparrow v. United States, 402 F.2d 826 (10th Cir. 1968) and United States v. Boyer, 694 F.2d 58, 60 (3rd Cir. 1982), offer no help. Sparrow was overruled by Hochfelder to the extent it rejected a good faith defense. See 425 U.S. at 211 n.31; Dirks, 463 U.S. at 674 n.11. Boyer recognized scienter as "the substantive element of the offense." 694 F.2d at 60. The scienter requirement functions in part "to protect good faith errors." Dirks, 463 U.S. at 674 n.11.

[9]This refusal, and the trial court's refusal to instruct the jury concerning the independent element of scienter, was reversible error. See State v. Jones, 823 P.2d 1059, 1061 (Utah 1991) (the absence of an instruction on all elements necessary to convict is "reversible error as a matter of law.") Mr. Larsen's requested (but refused) instructions, which cited Hochfelder, were plainly "sufficient to apprise the court of the theory of defense." Stapleman v. State, 680 P.2d 73, 76 (Wyo. 1984); Larsen's Requested Instr. Nos. 4, 5, 30 (R. 1353-56, 1381).

section 61-1-1 with proof of "willfulness" alone and that only ignorance or mistake of fact which disproves *that* intent was a defense. Jury Instr. Nos. 14, 17, 17A (R. 1309, 1312-13). And, while willfulness is an element of proof for a criminal violation of Section 61-1-1 (as it is for Rule 10b-5, 15 U.S.C. § 77x), it does not encompass the separate element of scienter. Dirks, 463 U.S. at 663 n.23 (Scienter "is an *independent* element of a Rule 10b-5 violation.") (emphasis supplied).[10]

3. The Legislative Purpose of Section 61-1-1

The State chides Mr. Larsen for acknowledging a simple truth: to effectuate the general legislative purpose of the Utah Act -- "to coordinate the interpretation and administration of this chapter with the related federal regulation" -- the Utah Act and the related federal law "must" be similarly construed. State br. at 9-10, 18-19; § 61-1-1. The State does not explain how otherwise to interpret the Utah Act and related federal law to fulfill this purpose. And, while the State contends that Utah

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[10]This refutes the State's claim that the only culpable mental state required to establish securities fraud is "wilfully." State's br. at 16-17. Because no additional mental element is contained in the "plain language" of the statute, the State argues, no additional element is necessary. State's br. at 7-8. Section 61-1-21 requires that a person act wilfully before criminal penalties arise. The related federal legislation contains a very similar provision requiring that a person act "wilfully" before a criminal penalty may be imposed. See 15 U.S.C. § 77x. However, as previously explained, the United States Supreme Court has recognized that a showing of scienter is a separate and independent element of a Rule 10b-5 violation. Aaron 446 U.S. at 690-91.

courts are "free" to disregard the interpretation of the related federal regulation (State's br. at 19), the Court is guided in construing section 61-1-1 by "[t]he primary rule of statutory interpretation [which] is to give effect to the *intent* of the legislature in light of the *purpose* the statute was meant to achieve." Reeves v. Gentile, 813 P.2d 111, 115 (Utah 1991) (emphasis supplied). In short, the State's reliance on § 17(a) and cases construing § 17(a) instead of Rule 10b-5, is unfounded.

B. Scienter is an *Independent* Element

The State argues alternatively that congressional intent making scienter an element of Rule 10b-5, and the legislative purpose of the Utah Act should be ignored because the "plain language" of sections 61-1-1(2) and 61-1-21, read in isolation, seem to allow prosecution without proof of scienter.[11] State's br. at 7-10. As previously discussed, the State's argument ignores the congressional intent of the model for section 61-1-1 and it defeats the purpose of the Utah Act.

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[11]Specifically, the State says that nothing in the language "gives rise to an *intent to defraud* element," again incorrectly limiting its definition of scienter to suit its analysis. State's br. at 7. Employing this narrow definition, the State cites several statutes containing the phrase "intent to defraud" and concludes that Utah's legislature never required proof of such intent unless the phrase "intent to defraud" expressly appears. State's br. at 10. However, even if this "survey" would permit the inference intended by the State, the inference cannot carry to the actual, broader definition of scienter the State ignores. See, e.g., Hochfelder, 425 U.S. at 193 n.12.

The Supreme Court in Hochfelder rejected a similar argument. The Securities and Exchange Commission argued that Rule 10b-5(b) and (c) (with language like section 6-1-1(2) and (3)), standing alone, could encompass intentional and negligent conduct. 425 U.S. at 212. The Hochfelder Court, however, held that scienter "is an *independent* element of a Rule 10b-5 violation." Dirks, 463 U.S. at 663 n.23 (citing to Hochfelder) (emphasis supplied). This interpretation is based largely upon the congressional intent of § 10(b) of the 1934 Act, the enabling legislation for Rule 10b-5. Hochfelder, 425 U.S. at 201 (§ 10(b) was intended by Congress to address "practices that involve some element of scienter . . ."); Aaron, 446 U.S. at 691. The scope of Rule 10b-5 does not exceed the power granted by Congress under § 10(b). 446 U.S. at 691. Thus, even though the language of Rule 10b-5(b), like section 61-1-1(2), when viewed alone, could be "read as prescribing . . . any type of material misstatement or omission, and any course of conduct, that has the effect of defrauding investors, whether the wrongdoing was intentional or not," Hochfelder, 425 U.S. at 212, violations were intended to require proof of scienter. Id. See also Aaron, 446 U.S. at 700 ("In the *absence* of a conflict between reasonably plain meaning and legislative history, the words of the statute must prevail.") (emphasis supplied).

This interpretation is consistent with considerations of policy that the State overlooks. Petitioner's brief at 16-18. Even in the context of a civil action, the Supreme Court in Hochfelder was troubled that by accepting the view that scienter was unnecessary, the Court "would extend to new frontiers the 'hazards' of rendering expert advice under the Acts, raising serious policy questions not yet addressed by Congress." Hochfelder, 425 U.S. at 214 n.33. The Hochfelder court noted that it was not "the first court to express concern that the inexorable broadening of the class of plaintiff who may sue in this area of the law will ultimately result in more harm than good." Id. The scienter requirement abates these significant concerns.

While the State does not question these concerns, it denies that the interpretation it urges has a strict liability effect. State's br. at 21. However, other courts correctly recognize that the State's position imposes "a form of strict liability." People v. Mitchell, 175 Mich. App. 83, 437 N.W.2d 304, 308 (1989), citing Van Duyse v. Israel, 486 F. Supp. 1382, 1387 (E.D. Wis. 1980) (emphasis removed).

Section 61-1-1 was patterned after Rule 10(b)-5, "the logical model" for the Uniform Act. Louis B. Loss, Commentary on the Uniform Securities Act, 7 (1976). By adopting the Uniform Act, Utah's legislature made possible "the interchangeability of

judicial precedents in this important area." See Wallace F. Bennett, Securities Regulation in Utah: A Recap of History and the New Uniform Act, 1963 Utah L. Rev. 216, 232 n.112. This is plainly contemplated by the express purpose of the Uniform Act -- "to coordinate the interpretation and administration of this chapter with the related federal regulation." Utah Code Ann. § 6-1-27. Federal court interpretation of Rule 10b-5 should apply to section 61-1-1 in order to advance this purpose. Id.[12]

II. The Court of Appeals Misapplied the Law Concerning Expert Witness Testimony

A. The Court of Appeal's Reliance on Lueben is Mistaken

The State concedes that in reviewing the trial court's decision to admit Sherwood Cook's testimony, the "Court of Appeals relied heavily" on United States v. Lueben, 812 F.2d 179 (5th Cir. 1987) ("Lueben I").[13] Indeed, Lueben I forms the

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[12]The State's reliance on cases construing provisions other than section 61-1-1 is flawed first because the intent for section 61-1-1 is found in its express legislative purpose and known model which requires scienter, not in the language of the different statutes these cases construe. See State v. Delmotte, 665 P.2d 1314, 1325 (Utah 1983) (construing bad check statute); State v. Bergwerff, 777 P.2d 510, 511 (Utah App. 1989) (construing arson statute). And, again the State incorrectly limits its scienter analysis to cases addressing only "intent to defraud." State's br. at 8-9.

[13]The Court of Appeals reviewed the trial court's ruling under a "clear showing of abuse" standard. State v. Larsen, 828 P.2d 487, 492 (Utah App. 1992). This standard of review apparently accorded even greater deference to the trial court's decision than the simple abuse-of-discretion standard advanced by (continued...)

basis for the Court of Appeals' opinion. Yet, the entire analysis in Lueben I adopted by the Court of Appeals was vacated by United States v. Lueben, 816 F.2d 1032, 1033 (5th Cir. 1987) ("Lueben II"). The State, by footnote, says that Lueben II was just a "modification" that "did not appear to disturb the substance" of Lueben I because it did not openly "criticize" the stricken analysis. State's br. at 25 n. 6. The truth is, by vacating that section of its prior decision, the United States Court of Appeals for the Fifth Circuit leveled ultimate criticism.

However, even if Lueben I had not been vacated, admitting Mr. Cook's testimony was improper under its analysis. The State characterizes Mr. Cook's testimony, not as a legal opinion, but "more akin to the opinion testimony on the factual question discussed in Lueben." State's br. at 27. This notion is refuted by comparing the testimony proffered in Lueben with Mr. Cook's sworn remarks.

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[13](...continued)
the State. State's br. at 28. In State v. Ramirez, 817 P.2d 774, 781 n. 3 (Utah 1991), the Court implied that in reviewing a decision admitting evidence, the standard of review is higher than simple abuse of discretion: "[w]hether a piece of evidence is admissible is a question of law, and we always review questions of law under a correctness standard," granting the trial court "some discretion." Under either standard, the trial court's incorrect decision falls beyond the realm of proper discretion.

The defendant in Lueben offered expert testimony concerning how savings and loan associations make real estate loans. 812 F.2d at 183. Out of the jury's hearing, the expert testified in substance that in making the type of loans at issue, a savings and loan association would look only to the value of the property securing the loan without considering the borrower's income, employment or net worth. Id. See also United States v. Lueben, 838 F.2d 751, 754 n.3 (5th Cir. 1988) (appeal on remand). The court found that "[t]he clear *inference* from this testimony is that the false financial statements and income tax returns supplied by Lueben were not 'material' to the savings and loan associations' decision to make the loans to Lueben." 812 F.2d at 183 (emphasis added). The expert did not say that any particular facts were or were not "material."

The Lueben Court first explained that "an expert may not express a conclusion of law," and that such conclusions were correctly excluded in Matthews v. Ashland Chemical, 770 F.2d 1303 (5th Cir. 1985), where the court held that an expert's answers to hypothetical questions would simply tell the jury what result to reach, allowing the expert to voice a legal conclusion concerning the proximate cause of the claimed injuries. Id. at 184. The court then contrasted the proffered testimony of Lueben's expert with the impermissible testimony in Ashland and another case, Owen v. Kerr-McGee Corp., 698 F.2d 236 (5th Cir. 1983), which

upheld the exclusion of expert testimony on the legal cause of an accident, explaining the difference this way:

> [W]e think that [the expert's] testimony falls within the permissible fact-oriented question. Lueben sought to ask [the expert] the factual question of whether the false statements in this case would have "the capacity to influence" a loan officer . . . not the legal question of whether the statements were "material."

Id. (emphasis added).

The fact-oriented testimony proffered in Lueben contrasts sharply with the legal opinion given by Mr. Cook:

> Q. Mr. Cook, let's take a situation where you have a limited partnership and there is an asset such as an interest in another limited partnership that is valued at approximately $175,000 that is given to the general partner by another individual in order to indemnify the general partner against his losses that he might incur as general partner of that limited partnership. Now, do you have an opinion as to whether or not in the offering documents those facts ought to be . . . disclosed in an offering document similar to that one?
>
> **A.** Yes, I would consider that material information. . . .
>
> **Q.** Let me put this question to you. Again, assume that you are looking at a limited partnership and a Private Placement Memorandum, and there was an investment manager that was supposed to make sure that certain criteria were fulfilled before loans were made from the limited partnership funds. And assume, if you will, that the investment manager never met, never operated, never exercised his prerogative or made a recommendation, would you want those facts disclosed in a disclosure document to investors.
>
> **A.** Objection. . . . (off the record discussion between Court and counsel).

Q. Mr. Cook, do you remember the facts and the hypothetical situation?

A. Would you ask it again?

Q. Let's suppose you were examining the limited partnership in which there is an investment manager that will make certain recommendations as to how money is going to be used from the limited partnership, specifically regarding certain loan criteria. And let's assume also that the investment manager never functioned, never made those recommendations and, in fact, ever met. Would you want those facts disclosed in a disclosure document to investors?

A. Yes, that would also be material.

(Transcript Vol. VI at 87-91)(emphasis added).

Thus, unlike the expert in Lueben, Mr. Cook did not just testify that certain information "would have the capacity to influence." Compare, Lueben, 812 F.2d at 184. Mr. Cook told the jury that the information was "material" and should have been disclosed. (Transcript Vol. VI at 87-91). In effect he told the jury that Mr. Larsen was guilty.[14]

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[14] Cook's conclusions also reveal that the Court of Appeals' remark that Mr. Cook used the term "material" in a "factual sense" is unfounded. State v. Larsen, 828 P.2d 487, 493 (Utah App. 1992). Cook's testimony confirms that Mr. Cook, the lawyer and securities regulator, used the term "material" as an improper legal conclusion, basing his opinions on hypothetical facts. See Specht v. Jensen, 853 F.2d 805, 808-09 n.5 (10th Cir. 1988), cert. denied, 488 U.S. 1068 (1989). (Error to allow attorney-expert witness to testify as to legal conclusions. "The expert in the instant case did not testify on issues of fact because he based his opinions on hypothetical facts. The expert added nothing to resolve the salient factual issues.") And the State does not question that as both an attorney and top securities regulator who had previously investigated Mr. Larsen, the error

(continued...)

Lueben I condemned such testimony. Id. at 184, citing Ashland, 770 F.2d at 1311 ("[T]he expert's answers to hypothetical questions posed in that case would simply tell the jury what result to reach and would allow the expert to voice a legal conclusion.") In sum, even under the vacated Lueben I analysis upon which the Court of Appeals depends, the Court of Appeals' decision condoning the admission of Cook's testimony was incorrect.

Notwithstanding the Court of Appeals mistaken reliance on Lueben I, the State attempts to justify the result of the court's decision, suggesting that Mr. Cook's testimony is admissible under State v. Span, 819 P.2d 329 (Utah 1991) (expert opined that fire had been intentionally set), United States v. Buchanan, 787 F.2d 477 (10th Cir. 1986) (officer of Bureau of Alcohol, Tobacco, and Firearms allowed to testify that a device was a firearm subject to registration with the Bureau), and United States v. Logan, 641 F.2d 860 (10th Cir. 1981) (expert testified that funds were wrongfully taken from corporation). State's br. at 28. However, the court in Scop v. United States, 846 F.2d 135, modified on rehearing, 856 F.2d 5 (2d Cir. 1988), made an important distinction between such cases, where experts

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[14](...continued)
of allowing Mr. Cook's testimony was so prejudicial that it could not have been corrected. 853 F.2d at 808; Marx & Co., Inc. v. Diners' Club, Inc., 550 F.2d 505, 511 (2d Cir), cert. denied, 434 U.S. 861 (1971).

had been allowed to testify as to certain legal conclusions, and cases like this. 846 F.2d at 141, citing, e.g., United States v. Young, 745 F.2d 733 (2d Cir. 1984), cert. denied, 470 U.S. 1084 (1985) (police detective allowed to testify that narcotics transaction had taken place). The Scop court explained that the testimony in cases like those cited here by the State, though perhaps still offensive, was permissible because it did not repeatedly use statutory or regulatory language indicating guilt. Scop, 846 F.2d at 141-42.

> [T]elling the jury that a defendant acted as a "steerer" or participated in a narcotics transaction differs from opining that the defendant "possessed narcotics, to wit, heroin, with the intent to sell," or "aided and abetted the possession of heroin with intent to sell," the functional equivalent of Whitten's testimony in a drug case.

Id. at 142. This distinction exists here. Mr. Cook, as explained above, did not simply testify that certain information could influence investors. He recited the key statutory term and said the information was "material."

B. Scop Provides Correct Analysis

The State attempts to distinguish Cook's testimony from the testimony condemned in Scop, Adalman[15] and Marx[16]. Yet, the State does not question the correctness of the rule these cases

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[15]Adalman v. Baker, Watts & Co., 807 F.2d 359 (4th Cir. 1986).

[16]Marx & Co., Inc. v. Diner's Club, Inc., 550 F.2d 505 (2d Cir.) cert. denied, 434 U.S. 861 (1977).

establish, or that cases of alleged securities fraud pose unique difficulties when testimony like Mr. Cook's is admitted, as Scop, Marx and Adalman explain. See Petitioner's br. at 20-23. The State simply concludes that these cases do not apply because Mr. Cook's testimony, "while it would have been better for [him] to steer away from the term 'material'", was free of "legal opinion." State's br. at 27. However, compared with Cook's testimony, the context and the testimony held improper in Scop seem indistinguishable.

The defendants in Scop were prosecuted for mail fraud, securities fraud and conspiracy. The government's expert witness was the chief investigator over for the SEC regional office and had been a stockbroker for eight years prior to joining the SEC. He also had personally spent over one thousand hours working on the Scop case. 846 F.2d at 138. Like Mr. Cook, who testified of his participation in a previous securities investigation of Mr. Larsen (Transcript Vol. VI at 47-52, Appendix E), the Scop expert did not testify as a witness with personal knowledge of relevant events. He testified as an expert in securities trading practices, purportedly basing his testimony only on the testimony and documentary evidence introduced at trial. 846 F.2d at 138. When the expert was asked whether there was a scheme to defraud investors, he was allowed to answer: "It is my opinion that the stock . . . was manipulated and that certain individuals were

active participants and material participants in the manipulation of that stock . . . ." Id. The Scop Court held that the expert's "repeated statements embodying legal conclusions exceeded the permissible bounds of opinion testimony" under the rules of evidence, noting that he drew directly upon the language of the statute concerning "manipulation" and "fraud." Id. at 138, 140.

Cook's testimony was no different. Mr. Cook's repeated statements embodied legal conclusions that certain information was "material"; it drew directly upon the language of the statute (see Utah Code Ann. § 61-1-1 (1989)); it exceeded the permissible scope of expert opinion testimony. The trial court's decision admitting this testimony was incorrect and beyond the proper bounds of discretion.

CONCLUSION

For the above reasons, the Court should reverse the decision of the Court of Appeals and trial court and remand for new trial.

DATED this 8th day of March, 1993.

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CERTIFICATE OF SERVICE

I hereby certify that I caused a true and correct copy of the foregoing REPLY BRIEF OF THE PETITIONER to be hand delivered this 8th day of March, 1993, to the following:

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